International Seabed Authority ISBA/21/FC/5

Finance Committee

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Status of the International Seabed Authority Endowment Fund for Marine Scientific Research in the Area and possible options for its future management and investment

Report of the Secretary-General

I. Introduction

1. The purpose of the present document is to inform the Finance Committee of the status of the International Seabed Authority Endowment Fund for Marine Scientific Research and, in response to concerns expressed by the Advisory Panel for the Endowment Fund at its twelfth meeting in February 2015, to identify possible alternatives for managing and investing the Endowment Fund in order to ensure that it is able, both now and in the foreseeable future, to meet the objectives for which it was established.

II. Background information

2. The International Seabed Authority Endowment Fund for Marine Scientific Research in the Area was established by the Assembly by resolution ISBA/12/A/11, adopted on 16 August 2006, with a view to implementing article 143, paragraph 2, of the United Nations Convention on the Law of the Sea, which provides that the International Seabed Authority shall promote and encourage the conduct of marine scientific research in the Area. In the resolution, the Authority decided that the purpose of the Fund should be to promote and encourage the conduct of marine scientific research in the Area for the benefit of mankind as a whole, in particular by supporting the participation of qualified scientists and technical personnel from developing countries in marine scientific research programmes and by providing them with opportunities to participate in international technical and scientific cooperation, including through training, technical assistance and scientific cooperation programmes. Detailed rules and procedures for the administration and utilization of the Fund are set out in a decision adopted by the Assembly on 19 July 2007 (ISBA/13/A/6, annex).

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3. Applications for assistance from the Endowment Fund may be made by any developing country or by any other country, if the purpose of the grant is to benefit scientists from developing countries. Pursuant to the agreed procedures, an Advisory Panel is to be appointed by the Secretary-General to evaluate applications for assistance from the Fund and make recommendations to the Secretary-General. Appointments to the Advisory Panel are for a period of three years.

III. Status of the Endowment Fund

4. As at 31 May 2015, the capital of the Endowment Fund stood at $3,455,538. From the start of the Fund up to 31 May 2015, a total amount of $480,081 had been disbursed from the interest accrued on the capital in the form of awards to support qualifying projects. A total of 66 scientists or government officials from 36 developing countries/areas have been beneficiaries of financial support from the Endowment Fund: Argentina, Bangladesh, Bolivia (Plurinational State of), Brazil, Cameroon, China, Colombia, the Cook Islands, Costa Rica, Egypt, Fiji, Guyana, India, Indonesia, Jamaica, Madagascar, Maldives, Malta, Mauritania, Mauritius, Micronesia (Federated States of), Namibia, Nigeria, Palau, Papua New Guinea, Peru, the Philippines, the Russian Federation, Sierra Leone, South Africa, Sri Lanka, Suriname, Thailand, Trinidad and Tobago, Tunisia and Viet Nam. The status of the Fund is detailed in the annex to the present report.

IV. Current challenges facing the fulfilment of the objectives of the Endowment Fund

5. Despite the achievements of the Endowment Fund, challenges to fulfilling the purpose of the Fund remain. Some of the challenges were noted by the Advisory Panel at its twelfth meeting, in February 2015. The Panel noted that as a result of the current low interest rate environment, the Fund was generating less than 1 per cent interest and was therefore not keeping pace with the rate of inflation or the costs of marine scientific research. Were the current recommendations of the Panel to be followed, the funding available for projects would be entirely exhausted in 2015. The Panel recommended that the Finance Committee should give consideration to alternatives for investing and managing the Fund so that it could grow in real terms.

6. The primary concern with respect to the Endowment Fund is the low interest income earned by the Fund as a result of the low interest rate environment. The interest generated is shown in table 1 below.

Table 1
Balance and interest income history of the International Seabed Authority Endowment Fund
(United States dollars)

Date	*Fund balance*	*Interest income*	*Interest rate (per cent)*
31 December 2011	3 385 009	4 961	0.15
31 December 2012	3 413 604	26 815	0.79
31 December 2013	3 452 424	63 903	1.87
31 December 2014	3 483 019	33 812	0.98
2015 (up to 31 May 2015)	3 481 920	13 780	0.41 (approximately 0.9 annual)

7. In 2012, the Finance Committee took note of the higher interest rates offered by the Bank of Nova Scotia Jamaica Limited and recommended that the Secretary-General invest the capital of the Endowment Fund in that bank in short-term time deposits, in United States dollars.

8. First, while the amount of interest income increased in 2012 and 2013, it decreased in 2014 and is expected to stay at similar levels in 2015. The present challenge facing the Endowment Fund is that the current low interest rate environment results in low levels of interest income that are likely to be insufficient to fund future projects. For example, in February 2015, the Advisory Panel considered four project applications and recommended that the Secretary-General fund three applications for a total amount of up to $39,880. The amount required will likely exceed by approximately $8,540 the projected interest income of $31,340 to be earned by the Endowment Fund in 2015.

9. Second, at current interest income levels, the Endowment Fund is not keeping pace with the rate of inflation or the costs of the marine scientific research that it is funding. For the long-term sustainability and viability of the Fund, consideration should be given to growth and the preservation of inflation-adjusted capital in selecting investment options.

10. The third challenge is the low level of contributions to the capital of the Endowment Fund. Between the previous session of the Authority in 2014 and 31 May 2015, only two contributions were received: from Mexico ($7,500) and from Tonga ($1,000). It is very difficult to encourage contributions to the capital of a fund that is constrained in its operations by extremely low interest rates. It is to be noted that from 2010 through 2014, the average annual contribution was $43,050, while the average annual amount disbursed from 2008 to date was $60,010. This is not sustainable in the long term.

V. Options for increasing available funds from the Endowment Fund

11. In order to increase the number and total value of applications funded, the two available options are:

(a) To modify the decision of the Assembly of 19 July 2007 so that the Endowment Fund may spend part of its capital;

(b) To increase the income earned by the Endowment Fund.

12. Clearly, the first option is only a short-term option, since income will gradually decrease along with the capital of the Fund. In addition, to spend the capital would necessitate a change in the decision of the Assembly of 19 July 2007, which would require the approval of the Council and the Assembly.

13. With little added risk, it may be possible to earn more than the approximately 0.9 per cent return currently earned by the Endowment Fund, for example, by investing in United States government bonds, which, on the basis of current interest rates, would yield the projected results indicated in table 2.

Table 2
Projected results of investment in United States government bonds at current interest rates
(United States dollars)

Term	*Interest rate*	*Current interest income for one year at 0.9 per cent*	*Projected interest income from United States government bonds*	*Projected additional (negative) income from United States government bonds*
1-month bill	0.010%	31 347	348	(30 999)
3-month bill	0.010%	31 347	348	(30 999)
6-month bill	0.079%	31 347	2 752	(28 595)
1-year note	0.222%	31 347	7 732	(23 615)
2-year note	0.572%	31 347	19 923	(11 424)
3-year note	0.929%	31 347	32 357	1 010
5-year note	1.486%	31 347	51 758	20 411
7-year note	1.874%	31 347	65 272	33 925
10-year note	2.139%	31 347	74 502	43 155
30-year bond	2.893%	31 347	100 764	69 417

Source: *Wall Street Journal*, 8 May 2015.

14. Given the higher rates obtainable from investing in United States government bonds, the Endowment Fund could consider buying 10-year notes, which would result in an additional 1.2 per cent per year of interest income. The investment of the current Endowment Fund balance of $3,481,920 would result in annual interest income of approximately $74,500, or approximately $43,053 more income than is currently being earned.

15. Alternatively, the Endowment Fund could increase its risk and potential long-term returns by hiring an outside investment manager with a mandate to invest globally, including in equities, real estate and fixed-income instruments. The 10-year (1 January 2005 to 31 December 2014) return on the Standard and Poors 500 Total Return Index, including dividends, was 7.6 per cent. This return exceeded the rate of inflation and included the negative returns earned during the 2007/08 financial crisis. This suggests that investing a portion of the Fund in equities could yield a higher income and grow the Fund in real terms, while also increasing its volatility. Nonetheless, given its long-term objectives, it is recommended that the Fund should be invested in longer-term assets instead of short-term time deposits as

at present to achieve a financial match between the long-term objectives of the Fund and its investment horizon.

16. This option would be in line with the provisions of financial regulation 9 on investment of funds, which provides as follows:

> 9.1 The Secretary-General may make short-term investments of a non-speculative nature, not needed for immediate requirements and shall inform the Finance Committee periodically of such investments which he or she has made.
>
> 9.2 The Secretary-General may, after consultations with an investment counsellor appointed on the recommendation of the Finance Committee, make long-term investments of moneys standing to the credit of trust funds, reserve and special accounts, except as may be otherwise provided by the appropriate authority in respect of each such fund or account and having regard to the particular requirements as to the liquidity of funds in each case.

17. It may be noted that another United Nations fund, the United Nations Joint Staff Pension Fund, has a long-term objective to generate a real return of 3.5 per cent over time. In its efforts to achieve this objective, the Pension Fund selectively engages the services of external fund managers who execute specialty investment mandates.

VI. Recommendations

18. The Finance Committee is invited to take note of the status of the Endowment Fund. The Committee is further invited to consider possible ways in which the income from the Fund may be increased to enable it to meet its objectives and, in particular, to consider the following options identified in the present document:

(a) To recommend that the Secretary-General take steps to invest the whole or part of the Endowment Fund in United States government bonds;

(b) To recommend that the Secretary-General appoint an investment counsellor pursuant to financial regulation 9, with a view to making appropriate long-term investments of all or part of the Endowment Fund. Given the relatively small size of the Fund, this will be subject to acceptance by a suitable investment counsellor;

(c) To recommend that the decision of the Assembly of 19 July 2007, in which it adopted the terms of reference, guidelines and procedures of the Endowment Fund (ISBA/13/A/6) be modified so that the Fund may spend a portion of its capital.

Annex

Status of the International Seabed Authority Endowment Fund for Marine Scientific Research in the Area

International Seabed Authority
Status of the Endowment Fund as of 31 May 2015

Endowment Fund	
Capital	
Initial capital as of 18 August 2006	**2 631 803**
United Kingdom of Great Britain and Northern Ireland contribution, 16 May 2008	29 800
Mexico contribution, 6 October 2008	2 500
Spain contribution, 5 November 2008	25 514
Norway contribution, 25 August 2009	250 000
Germany application fee + interest as of 25 September 2009	276 719
United Kingdom of Great Britain and Northern Ireland contribution, 22 March 2010	15 253
Interest not spent as of 31 December 2009	**16 535**
Interest not spent as of 31 December 2010	**6 414**
Nigeria contribution, 22 June 2011	10 000
Mexico contribution, 7 September 2011	2 500
Japan contribution, 15 September 2011	100 000
United Kingdom of Great Britain and Northern Ireland contribution, 17 January 2012	20 000
Mexico contribution, 8 November 2012	5 000
United Kingdom of Great Britain and Northern Ireland contribution, 18 July 2013	10 000
Mexico contribution, 10 September 2013	5 000
United Kingdom of Great Britain and Northern Ireland contribution, 24 April 2014	10 000
Republic of Korea contribution, 3 July 2014	30 000
Mexico contribution, 4 September 2014	7 500
Tonga contribution, 18 December 2014	1 000
Total capital	**3 455 538**
Interest	
Earned in 2006	49 826
Earned in 2007	125 248
Earned in 2008	100 540
Earned in 2009	44 007
Earned in 2010	44 018
Earned in 2011	4 961
Earned in 2012	26 815

Endowment Fund	
Earned in 2013	63 903
Earned in 2014	33 812
Earned in 2015	13 780
Total cumulated interest	**506 910**
Expenditures	
Contribution to InterRidge, December 2008	(30 000)
Contribution to Voluntary Trust Fund, December 2008	(20 000)
Contribution to E&F Shared Resources Centre (Rhodes Academy), May 2009	(35 146)
Contribution to National Institute of Oceanography, India, September 2009	(14 700)
Contribution to Duke University, United States of America, October 2009	(41 456)
Flight cost for National Institute of Oceanography participants	(4 499)
Contribution to Rhodes Academy, May 2009	(29 273)
Contribution to National Institute of Oceanography, India, October 2010	(19 600)
Flight cost for National Institute of Oceanography participants, October-December 2010	(10 851)
Contribution to E&F Shared Resources Centre (Rhodes Academy), December 2010	(30 000)
Contribution to Voluntary Trust Fund, December 2010	(40 000)
Contribution to Rhodes Academy, December 2011	(30 000)
Contribution to InterRidge, December 2011	(45 000)
Bank expenditures	(447)
Contribution to International Network for Scientific Investigation of Deep-Sea Ecosystems (INDEEP)	(18 000)
Contribution to E&F Shared Resources Centre (Rhodes Academy), April 2013	(15 000)
Contribution to Second Institute of Oceanography (Southwest Indian Ridge), April 2013	(15 000)
Contribution to E&F Shared Resources Centre (Rhodes Academy), 2nd instalment, November 2013	(15 000)
Contribution to E&F Shared Resources Centre (Rhodes Academy), 1st instalment, April 2014	(15 000)
Flight cost for A. Wasuwatcharapong (conducted by Task Group for the Portuguese Continental Shelf Extension (EMEPC))	(1 257)
Contribution to E&F Shared Resources Centre (Rhodes Academy), 2nd instalment, September 2014	(15 000)
Contribution to Second Institute of Oceanography (Southwest Indian Ridge), December 2014	(20 420)
Contribution to Southampton INDEEP/ISA travel bursary to Deep-Sea Biology Society Applications	(14 880)
Total expenditures	**(480 528)**
Available funds to be used (interest - expenditures)	**26 382**
Initial capital + interest - expenditures as of 31 May 2015	**3 481 920**

Annual interest gained analysis

Year	*Inversion US$*	*Annual interest gained US$*	*Annual interest rate %*
2006	2 631 803	49 826	1.89%
2007	2 681 629	141 783	5.29%
2008	2 801 426	106 954	3.82%
2009	3 326 560	44 007	1.32%
2010	3 291 694	44 018	1.34%
2011	3 335 712	4 961	0.15%
2012	3 387 038	26 815	0.79%
2013	3 387 038	63 903	1.89%
2014	3 387 038	33 812	1.00%
2015	3 387 038	13 780	0.41%
Average annual rate	**3 528 742**	**66 232**	**1.88%**